BEFORE THE

PUBLIC UTILITIES COMMISSION
OF THE
STATE OF RHODE ISLAND
AND PROVIDENCE PLANTATIONS

IN THE MATTER OF

The National Grid Proposal	**)**	
For Changes In Its Distribution	**)**	**Docket No. 3760**
Adjustment Charge	**)**	

DIRECT TESTIMONY OF WITNESS BRUCE R. OLIVER

On Behalf of

The Division of Public Utilities and Carriers

October 13, 2006

TESTIMONY OF BRUCE R. OLIVER
Docket No. 3760
October 13, 2006

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS FOR THE RECORD.

A. My name is Bruce R. Oliver. My business address is 7103 Laketree Drive, Fairfax Station, Virginia, 22039.

Q. BY WHOM AND IN WHAT CAPACITY ARE YOU EMPLOYED?

A. I am employed by Revilo Hill Associates, Inc., and serve as President of the firm. I manage the firm's business and consulting activities, and I direct its preparation and presentation of economic, utility planning, and policy analyses for our clients.

Q. ON WHOSE BEHALF DO YOU APPEAR IN THIS PROCEEDING?

A. My testimony in this proceeding is presented on behalf of the Division of Public Utilities and Carriers (hereinafter "the Division").

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. This testimony addresses the request of National Grid (hereinafter “NG” or “the Company”) for a change in its Distribution Adjustment Charge (“DAC”) which is set forth in testimony filed on August 1, 2006 and September 1, 2006 by witness Peter C. Czekanski on behalf of the Company. More specifically, this testimony discusses all elements of the Company’s DAC calculations other than the Earnings Sharing

Mechanism. Issues relating to Earnings Sharing for the 12 months ended June 30, 2006 will be addressed in the testimony of Division witness David Effron.

Q. AT PAGES 2-3 OF HIS SEPTEMBER 1, 2006 SUPPLEMENTAL TESTIMONY, WITNESS CZEKANSKI ADDRESSES THE NATIONAL GRID PURCHASE OF NEW ENGLAND GAS COMPANY'S RHODE ISLAND OPERATIONS. DO YOU AGREE WITH MR. CZEKANSKI THAT THE RESULTING ORGANIZATIONAL CHANGE SHOULD HAVE NO IMPACT ON THE COMMISSION'S CONSIDERATION OF THIS FILING?

A. Yes, I do. For the purposes of the non-Earnings Sharing considerations in this proceeding, the transition from New England Gas Company to National Grid should be seamless. Also, in that context, it should be understood that any reference to "the Company" or to data for "the Company" for periods prior to August 24, 2006 addresses New England Gas Company operations or data.

Q. WHAT IS THE DAC RATE THAT THE COMPANY PROPOSES IN THIS PROCEEDING?

A. Attachment PCC-1 to the Company's August 1, 2006 filing computes an overall DAC rate of $0.0018 per therm. Updated Attachment PCC-1 which is presented as part of witness Czekanski's September 1, 2006 testimony in this proceeding computes

an overall DAC rate of $0.0003 per therm. By comparison, the Company's present DAC rate is a ($0.0031). Thus, the DAC rate computed in the Company's September 1, 2006 filing reflects an **increase** of **$0.0034** per therm from the currently effective DAC rate.

Q. WHAT ARE THE MAJOR COMPONENTS OF THE COMPANY'S DISTRIBUTION ADJUSTMENT CHARGE (DAC) CALCULATIONS?

A. NG's proposed DAC calculations comprise nine (9) major components. The components of the Company's Distribution Adjustment Charge calculations include:

1. A System Pressure (SP) Factor
2. A Demand Side Management (DSM) Factor
3. A Low Income Assistance Program (LIAP) Factor
4. An Environmental Response Cost (ERC) Factor
5. An On-System Margin Credits (MC) Factor
6. A Weather Normalization (WN) Factor
7. An Earnings Sharing Mechanism (ESM)
8. A Reconciliation (R) Factor
9. An Allowance for Uncollectibles

The first eight components of the Company's DAC calculations are re-examined, and subject to re-calculation on an annual basis. The last component (i.e., the Allowance for Uncollectibles), was established through the Commission-approved settlement in Docket No. 3401. The Reconciliation (R) Factor includes adjustments for over- or under-recovery of costs during the 12-months ended June

30, 2006 for each of the first eight factors listed above. NG's proposed calculations for each of the components of the DAC are reviewed below.

System Pressure Factor

Q. WHAT IS THE PURPOSE OF THE SYSTEM PRESSURE ADJUSTMENT?

A. Since the beginning of rate unbundling for firm service customers, this Commission has recognized that a portion of the Company's use of its LNG facilities is associated with the maintenance of operating pressures on its system. Given that both sales service and transportation service customers benefit from the maintenance of system operating pressures, it is appropriate that such costs be recovered from customers in both of those service classifications. In the absence of the System Pressure Adjustment, all of the Company's LNG costs would be recovered through its Gas Cost Recovery (GCR) charges and paid for by only sales service customers. Thus, it is necessary for the Company to allocate a portion of its LNG costs to system pressure maintenance, and collect those costs through charges that are applied to both firm sales service and firm transportation service customers. The System Pressure factor within the DAC mechanism accomplishes this objective.

Q. HOW IS THE SYSTEM PRESSURE FACTOR DETERMINED?

A. As established in Docket No. 3401, the System Pressure factor is computed by multiplying Total LNG Commodity Related Costs by the System Balancing Factor (.2039) and dividing by projected, weather-normalized, annual Firm Throughput. The .2039 factor reflects the results of an assessment which suggested that 20.39% of LNG commodity related costs were used for System Pressure purposes, and therefore, should be borne by all customers (i.e., sales and transportation service customers) who utilize the Company's distribution system.

Q. WHAT IS THE LEVEL OF THE SYSTEM PRESSURE FACTOR THAT NG PROPOSES IN THIS PROCEEDING BASED ON DATA FED JUNE 30, 2006?

A. Attachment PCC-2 to Mr. Czekanski's testimony filed July 30, 2006 computes a System Pressure Factor of $0.0589 per Dth. The data used in those calculations were subsequently updated in Mr. Czekanski's September 1, 2006 Updated Attachment PCC-2. Based on its updated calculations, NG now seeks a System Pressure Factor of $0.0537 per Dth. The difference between these results is noticeable, but not dramatic. However, the changes in the monthly costs that underlie the Company's System Pressure Factor calculations are substantial, particularly considering that these filing were made just one month apart. These differences appear to be directly related to declines in NYMEX natural gas

commodity costs for the coming winter period since the prices NG pays for LNG are indexed to NYMEX natural gas prices and NYMEX natural gas prices have fallen sharply between the Company's August 1 and September 1 filings.

Q. IS THE COMPANY'S UPDATED SYSTEM PRESSURE FACTOR APPROPRIATELY COMPUTED?

A. The Company's updated System Pressure Factor computations are mathematically accurate.

Q. ON JULY 29, 2005 THE NEW ENGLAND GAS COMPANY FILED AN "LNG SYSTEM PRESSURE REPORT" IN DOCKET NO. 3458 WHICH OUTLINED A PROCEDURE FOR ADDRESSING LNG THAT MAY BE USED FOR ECONOMIC DISPATCH PURPOSES IN FUTURE FILINGS. DO YOU FIND EVIDENCE THAT NG HAS PROPERLY EXCLUDED LNG USED FOR ECONOMIC DISPATCH PURPOSES FROM THE LNG COSTS THAT IT USES TO COMPUTE ITS UPDATED SYSTEM PRESSURE FACTOR?

A. Neither the August 1, 2006 version of Attachment PCC-2 nor the subsequent September 1, 2006 update of that attachment includes any reference to, or documentation of, the exclusion of economically dispatched LNG volumes from costs used to compute the Company's System Balancing Costs for the twelve

months ended October 31, 2006. However, through informal discovery with Mr. Czekanski I learned that the Company reviewed its LNG use over the past winter season and found no use of LNG for economic dispatch purposes. Thus, the data used by NG in its System Pressure Factor calculations appear to be appropriate.

Demand Side Management Factor

Q. WHAT IS THE PURPOSE OF THE DEMAND SIDE MANAGEMENT FACTOR?

A. The Demand Side Management Factor provides the Commission a mechanism for adjusting NG's DSM Funding outside the context of a base rate proceeding.

Q. WHAT IS THE LEVEL OF FUNDING CURRENTLY PROVIDED FOR DSM PROGRAMS THROUGH THE COMPANY'S BASE RATES?

A. As set forth in NG's tariff, Section 3, Distribution Adjustment Charge, Schedule A, Sheet 3, paragraph 3.2, the DSM funding presently embedded in base rates for NG is **$301,496** per year. That tariff amount includes an allowance for working capital. The actual amount provided through rates to fund DSM payments to customers is $300,000.

Q. WILL ANY DSM FUNDS BE CARRIED FORWARD FROM FY 2006?

A. Yes. The Company had a carry forward balance of uncommitted DSM funds at the end of FY 2006 of $41,388. In addition, NG represents that it has $305,267 of funds committed to three already approved projects that are awaiting full implementation. Thus, the total estimated carry forward balance for DSM costs is $346,655. To that amount the Company adds $300,000 of expected annual funding through base rates to arrive at total funding for DSM programs during FY 2007 of $646,655.[1] However, after subtracting funds that have been committed to already approved projects, the funding available for new projects is $341,388.

Q. IS THE COMPANY PROPOSING ANY CHANGE IN FUNDING FOR DSM PROJECTS FOR FY 2007?

A. No. As a result the Demand Side Management (DSM) factor for the coming year remains $0.0000 per therm.

Q. DO RATEPAYERS EARN INTEREST ON THE UNEXPENDED BALANCE OF DSM FUNDS?

[1] The Company's tariff at Section 3, Distribution Adjustment Charge, Schedule A, Sheet 4, paragraph 3.2 actually provides for $301,496 of funding for DSM programs through base rates. However, that amount includes an allowance for working capital. The referenced $300,000 of new funding for DSM projects is the amount that remains after the working capital allowance is subtracted.

A. Yes. The computation of interest on the unexpended balance of DSM funds is shown on page 2 of Attachment PCC-7, as well as on page 2 of Updated Attachment PCC-7.

Low Income Assistance Program Factor

Q. WHAT IS THE PURPOSE OF THE LOW INCOME ASSISTANCE PROGRAM (LIAP) FACTOR?

A. The Low Income Assistance Program (LIAP) Factor performs a function similar to that of the DSM Factor. It provides a mechanism for the Commission to adjust the funding of the Company's Low Income Heating Assistance Program (LIHEAP) and Low Income Weatherization Program activities outside the context of a base rate proceeding.

Q. WHAT IS THE LEVEL OF FUNDING CURRENTLY PROVIDED FOR NG'S LOW INCOME ASSISTANCE PROGRAMS THROUGH ITS BASE RATE CHARGES?

A. As set forth in the Company's tariff, Section 3, Distribution Adjustment Charge, Schedule A, Sheet 4, paragraph 3.3, the DSM funding presently embedded in base rates for NG is **$1,793,901** per year. As noted above for DSM funding, the dollar

amount stated in the Company's tariff includes an allowance for working capital. After subtracting the working capital allowance the amount of new LIHEAP funding is $1,785,000.

Q. **ARE ANY FUNDS FOR LOW INCOME ASSISTANCE PROGRAMS BEING CARRIED OVER FROM FY 2006?**

A. Yes. The Company reports that $17,400 of LIHEAP funding will be carried over from FY 2006 to FY 2007. Thus, the total funds available for Low Income Assistance programs in FY 2007 will be $1,802,400.

Q. DOES NG SEEK ADDITIONAL LIAP FUNDING THROUGH ITS PROPOSED DSM FACTOR IN THIS PROCEEDING?

A. No, it does not. Therefore, the LIAP factor in the Company's DAC calculations remains at zero.

Environment Response Cost Factor

Q. PLEASE DESCRIBE THE PURPOSE OF THE ENVIRONMENTAL RESPONSE COST (ERC) FACTOR?

A. The primary function of the ERC Factor is to provide the Company a means of recovering "reasonable and prudently incurred" environmental response costs while limiting impacts on customers' bills. Costs subject to recovery through the ERC Factor include:

(1) Costs for evaluation, remediation and clean-up of sites associated with NG's ownership and operation of manufactured gas plants, manufactured gas storage facilities, and manufactured gas plant-related off-site waste disposal locations;

(2) Costs for removal and disposal of mercury regulators and meters; and

(3) Costs for acquiring property associated with the clean up of such sites;

(4) Litigation costs, claims, judgments, and settlements associated with environmental clean up activities.

Q. HOW ARE REASONABLE AND PRUDENTLY INCURRED ENVIRONMENTAL RESPONSE COSTS RECOVERED THROUGH THE ERC FACTOR?

A. According to the terms of the settlement approved by this Commission in Docket No. 3401, such Environmental Response Costs shall be recovered through a 10-year straight-line amortization, subject to the restriction that the ERC Factor shall be limited to an increase of no more than $0.01 per therm in any annual DAC filing. Moreover, the ERC Factor is computed to reflect an adjustment to the $1,310,000 of Environmental Response Costs that is presently included in NG's base rate charges. Thus, the dollar amount subject to recovery through the ERC Factor in any year reflects the sum of all applicable 10-year ERC amortizations less the $1,310,000 of budgeted base rate recoveries, and the ERC Factor reflects that net dollar amount divided by forecasted firm throughput.

Q. WHAT IS THE NET DOLLAR AMOUNT THAT NG PROPOSES IN THIS PROCEEDING FOR RECOVERY THROUGH ITS ERC FACTOR?

A. As shown in Attachment PCC-3, filed on August 1, 2005, the Company seeks approval of a net recovery of ($650,265). That net dollar amount reflects:

1. A 10-year amortization of $12,510,252 of net ERC costs incurred through the end of FY 2002;

2. A 10-year amortization of ($6,012,673) of net ERC costs for FY 2003;

3. A 10-year amortization of ($472,960) of net ERC costs for FY 2004;

4. A 10-year amortization of $136,707 of net ERC costs for FY 2005;

5. A 10-year amortization of $436,020 of net ERC costs for FY 2006; and

6. A deduction of $1,310,000 for budgeted base rate recovery of ERC costs during the annual period in which the proposed ERC Factor will be effective.

Q. WHAT IS NET BALANCE OF THE ENVIRONMENTAL REMEDIATION COSTS TO BE RECOVERED THROUGH THE COMPANY'S ERC FACTOR?

A. The Company projects a net balance of unrecovered Environmental Response Costs at the end of FY 2006 of $3,477,968.

Q. WHAT IS THE LEVEL OF THE ERC FACTOR THAT NG PROPOSES IN THIS PROCEEDING?

A. NG proposes an ERC Factor of ($0.0019) per therm. That represents a net credit to firm customers. The current ERC factor is also ($0.0019) per therm, after

rounding. Thus, after rounding, there is no change in the level of the ERC factor from last year to this year.

Q. WHAT ARE THE MAJOR ELEMENTS OF THE ENVIRONMENTAL RESPONSE COSTS THAT NG CLAIMS FOR FY 2006?

A. For FY 2006 NG claims a net Environment Response Cost of $436,020. Of that amount, $284,643 or more than 65% is comprised of costs associated with its program for removal and replacement of Mercury Seal Regulators (MSRs). Three additional projects account for over 80% of the remaining $151,377 of net expenditures for FY 2006. Those projects and their associated costs are as follows:

➢ Project 307	PCB Reg Pipe Abandonment	$49,249
➢ Project 782	Tidewater	$39,679
➢ Project 907	Envir Phase II @ Allens Ave	$38,410
➢ Project 700	18 & 21 Holders COR	$20,181
Total		$127,228

Q. DO YOU FIND ANY REASON TO QUESTION THE AMOUNT OF ENVIRONMENTAL RESPONSE COSTS FOR WHICH THE COMPANY SEEKS RECOVERY IN THIS PROCEEDING?

A. The Company claims an expense of $284,643 for removal and replacement of 59 MSRs, as well as real time vapor screening, follow-up testing, and remediation of one location. Compared to the Company's past experience these costs appear

high. The Company's FY 2006 Annual Environmental Report indicates at page 11 that in prior periods nearly 9,000 MSRs were replaced at a total cost of $1,255,930. That equates to roughly $140 per MSR. However, the Company's reported expenses for the 12 months ended June 30, 2006 (i.e., $284,643) reflect an average cost per MSR removed of $4,824.46.

Upon further investigation I have found that a large portion of the total costs incurred under this project heading were for remediation activities at one location where mercury was found near a location on a customer's premises where it is believed that a mercury regulator may have formerly been installed. Clean-up of that one site accounted for nearly $135,000 of contractor billings to this project during FY 2006 plus additional costs for the involvement of Company personnel. Mr. Czekanski indicated to me through informal discovery that the total cost of that clean-up effort was nearly $150,000.

But, even after allowing for the costs of that clean up effort, the average cost of the 59 MSR removals during FY 2006 appears to be in excess of $2,200 per MSR removed. That is still more than 15 times higher than the average cost of removals completed in prior periods. Most of that increase appears to be explained by increases in the Company's real time vapor screening and follow-up testing, as well as the involvement of contractor personnel in the transport of removed regulators to a facility in Braintree, MA. These activities are explained in NG's response to

Division Data Request 2-05, and the costs for those activities are reflected in the Clean Harbors entries on page 5 of Attachment DIV 2-05a.

Q. DO YOU PROPOSE ANY ADJUSTMENTS TO THE FY 2006 EXPENSES THAT NG SEEKS TO INCLUDE IN ITS ENVIRONMENTAL RESPONSE COST CALCULATIONS?

A. No, I do not. With the information provided in the Company's response to Division Data Request 2-05, the attachments to that response, and further clarifying information provided informally by Mr. Czekanski, I am satisfied that the Company's claimed environmental response costs for FY 2006 are reasonable and that the proposed ERC factor is appropriately computed.

On-System Margin Credits

Q. WHAT IS THE ROLE OF THE ON-SYSTEM MARGIN CREDIT (MC) FACTOR?

A. The On-System Margin Credit (MC) Factor performs two functions. First, it provides NG a mechanism for recovery of shortfalls, if any, in the actual on-system margin revenue derived from non-firm sales and transportation services relative to the $1.6 million of annual on-system margin revenue presently assumed in the design of the Company's base rates. Second, the MC Factor provides a mechanism for sharing

of on-system margin revenue in excess of the level assumed in the design of base rates. If actual non-firm margin revenue exceeds $1.6 million within the 12-month period ending June 30th of any year completed subsequent to the effective date of this tariff provision, the MC Factor provides an incentive to the Company to maximize such margin revenue by enabling NG to retain 25% of such revenue while crediting 75% of on-system non-firm margins to firm service customers as an offset to their distribution system costs.

Q. DID NG ACHIEVE ON-SYSTEM NON-FIRM MARGINS IN EXCESS OF $1.6 MILLION FOR THE 12-MONTH PERIOD ENDED JUNE 30, 2006?

A. Yes. Mr. Czekanski's August 1, 2006 testimony in this docket indicates that NG recorded non-firm margin revenue for the 12-months ended June 30, 2005 of $3,496,294. Thus, $1,896,294 of non-firm margin revenue was collected during that period in excess of the $1.6 million annual level on On-System Margin Revenue presently assumed in the design of NG's base rates. As required by the Company's tariff, 75% of that amount or $1,422,220 is subject to distribution as a credit to firm customers through the MC factor in the Company's DAC calculations. NG retains 25% or $474,073. The resulting On-System Margin Credit (MC Factor) per therm is $0.0041.

Q. WHAT EXPLAINS THE INCREASE IN THE LEVEL OF ON-SYSTEM MARGINS THAT NG ACHIEVED in FY 2006?

A. For most of the twelve month period ended June 30, 2006, the costs of fuel oil alternatives were well above those for natural gas. The pricing of non-firm services is based on the of the customer's alternative fuel cost. Thus, the Company's pricing of non-firm services permitted increased margins per therm of gas used by such customers. Although natural gas prices rose sharply following hurricanes Katrina and Rita in the latter part of calendar year 2005, they peaked in early December and have since fallen sharply. On the other hand, fuel oil prices have been slower to adjust downward, leaving rather large price differentials between the costs of natural gas and the costs of fuel oil. The resulting differentials between natural gas and fuel oil prices (viewed in terms of costs per MMBtu), allowed the Company to extract increased margins from non-firm customers during FY 2006.

Q. DO YOU FIND ANY REASON TO QUESTION THE ACCURACY OF THE COMPANY'S DETERMINATION OF ITS MARGINS ON NON-FIRM GAS SERVICE SERVICES FOR THE TWELVE MONTHS ENDED JUNE 30, 2006?

A. As of this time, I do not. Although I have not had the opportunity to review sufficient supporting detail for the Company's determination of its non-firm margins to draw any conclusion at this time regarding the accuracy and appropriateness of the

overall magnitude of the Company's non-firm margins, I am continuing my investigations and will attempt to provide a more definitive statement on that matter prior to hearings in this proceeding. Accepting *arguendo* the accuracy of the Company's representations regarding the total amount of the non-firm margins that it collected during FY 2006, NG's margin sharing calculations appear to be correct.

Weather Normalization

Q. WHAT IS THE INTENDED ROLE OF NG'S WEATHER NORMALIZATION FACTOR?

A. The Weather Normalization Factor provides a mechanism for moderating the impacts of weather on the Company's base revenue. When winter weather, as measured in Heating Degree Days (HDDs), is warmer than normal, NG's collection of fixed costs through its charges for distribution service declines below the level anticipated under normal weather conditions. If the resulting decline in heating degree days is significant, a positive Weather Normalization Factor is computed for the subsequent DAC period to compensate the Company for a portion of the revenue foregone due to reduced system throughput. On the other hand, colder than normal winter weather causes system throughput and distribution charge revenue to increase relative to expected revenue levels under normal weather

conditions. If recorded HDDs are greater than anticipated normal degree day levels, a negative Weather Normalization Factor (credit) returns a measure of excess revenue collections to customers during the subsequent DAC period.

However, the Weather Normalization Factor only addresses heating degree days recorded for each year that are more than 2% above or below normal heating degree day levels when accumulated over the defined winter season (i.e., the months of November through April). If recorded actual HDDs are within plus or minus 2% of normal levels for the winter season, no adjustment to revenue is permitted and the Weather Normalization Factor for the subsequent DAC period is zero. On the other hand, if total HDDs for the winter season are beyond the range defined by normal HDD expectations plus or minus 2%, each heating degree day beyond that range is multiplied by $9,000 per degree day to obtain the total dollar amount to be recovered from, or credited to, customers through the Weather Normalization Factor.

Q. WAS THE 2005-2006 WINTER SEASON A SUFFICIENTLY WARMER OR COLDER THAN NORMAL TO TRIGGER THE COMPUTATION OF A NON-ZERO WEATHER NORMALIZATION FACTOR FOR NG?

A. Yes. As shown in Attachment PCC-6 filed with Mr. Czekanski's August 1, 2006 testimony in this docket, the actual number of heating degree days (HDDs) for the

months of November 2005 through April 2006 was 4,579. Thus, actual heating degree days for that period were 199 HDDs below normal, and 103 HDDs below the threshold identified for computing making an upward adjustment to revenue for the Company (i.e., normal heating degree days less 2% or 4,682 HDDs).

Q. WHAT IS THE MAGNITUDE OF THE WEATHER NORMALIZATION FACTOR THAT RESULTS FROM THE WARMER THAN NORMAL WEATHER EXPERIENCED DURING THE WINTER OF 2005-06?

A. The Company's proposed Weather Normalization (WN) Factor is $0.0027 per therm. That factor is derived by multiplying the 103 HDDs (i.e., the number of HDDs in excess of the normal HDD level less 2%) by $9,000 per excess HDD. The product of that computation yields the previously mentioned $927,000 Weather Mitigation debit. Dividing that debit amount by the Company's projected Annual System Throughput for the November 2006 through October 2007 period of 34,893,906 dekatherms produces the proposed WN Factor.

Q. SHOULD THE COMMISSION ACCEPT THE COMPANY'S WEATHER NORMAL-IZATON (WN) FACTOR CALCULATIONS FOR THE 12 MONTHS ENDED OCTOBER 31, 2007?

A. Yes. The Commission should accept NG's Weather Mitigation computations and the resulting debit in the amount of $927,000. The Company's calculations supporting the determination of that debit have been performed in compliance with the procedures set forth in the Company's tariff, and are mathematically correct.

Reconciliation Factor

Q. HOW IS THE RECONCILIATION (R) FACTOR COMPUTED?

A. The Reconciliation (R) Factor component of the Company's DAC adjusts for differences between revenue collections associated with each component of DAC and either actual costs or budgeted revenue by component, adjusted for interest on deferred balances. In this proceeding, the R Factor computations include reconciling adjustments for Demand Side Management, Low Income Assistance, Environmental Response Costs, System Pressure, On-System Margin Credits, Weather Normalization, Earnings Sharing, and the previous Reconciliation Factor.

Q. WHAT IS THE RESULT OF NG'S R FACTOR COMPUTATIONS?

A. Updated Attachment PCC-7, page 1 of 9, reflects a Reconciliation Factor of ($0.0009) per therm for application in the Company's 2007. The R Factor, thus, results in a net credit to customers for the November 2006 – October 2007 period.

Q. ARE THE RECONCILING ADJUSTMENTS COMPUTED AS PART OF THE "R" FACTOR COMPONENT OF THE DAC REASONABLE AND APPROPRIATE?

A. Yes, I find that NG's reconciliation adjustments are accurately computed.

Distribution Adjustment Charge (DAC) Summary

Q. WHAT IS LEVEL OF THE DISTRIBUTION ADJUSTMENT CHARGE THAT NG PROPOSES IN THIS PROCEEDING?

A. The Company's proposed DAC charge is presented in Updated Attachment PCC-1 filed on September 1, 2005. That proposed DAC, including the adjustment of uncollectible accounts expense, represents a net charge of $0.0003 per therm for all firm customers.

Q. DO YOU PROPOSE ANY CHANGES TO DAC CALCULATIONS THAT NG HAS PRESENTED IN THIS PROCEEDING?

A. Not at this time.

Q. DO YOU HAVE ANY FURTHER COMMENTS REGARDING THE DAC CHARGE COMPUTATIONS THAT NG PRESENTS IN THIS PROCEEDING?

A. Between the Company's August 1, 2006 and September 1, 2006 filings in this proceeding, NG lowered its forecasted firm gas use from 34,893,906 Dth to 34,623,207 Dth (i.e., a 0.78% decrease). However, NG did not recompute each of its adjustment factors using the lowered gas use projection. Only the Updated System Pressure Factor, the Earnings Sharing Credit, and the Reconciliation (R) Factor were computed using the updated forecast of gas use. As a result, the Company's computed adjustment factors for Environmental Response Costs, On-System Margin Credits, and Weather Normalization are slightly misstated. Yet, the Company's failure to re-compute those components of its DAC charge has no material impact.

As long as there are no dramatic adjustments to NG's overall DAC charge and bills are computed using the dollars per therm charge proposed in Updated Attachment PCC-1 filed on September 1, 2006 (which uses only four decimal places) the impact of not re-computing the ERC, MC and WN factors is lost in rounding. However, if significant adjustments are made to DAC component factors and/or NG bills its DAC charges using dollars per therm computed to five decimal places, the amounts billed to customers could be slightly overstated. Schedule BRO-1 illustrates the potential impact of not re-computing the ERC, MC and WN factors using the Company's updated forecast of firm throughput.

Q. SHOULD ANY OTHER CHANGES BE MADE IN THE COMPANY'S DAC RECONCILIATIONS ON A GOING-FORWARD BASIS?

A. Yes. The Company's current DAC cost reconciliations apply the Bank of America Prime Rate to compute interest on over- or under-recovery balances. That approach to computing interest was adopted several years ago due to the unavailability of information regarding Southern Union's short-term costs of debt. However, the September 1, 2006 testimony of Sharon Partridge in this proceeding, Docket No. 3760, suggests that information regarding cost rates for short-term debt can be obtained. Moreover, the monthly cost rates for short-term debt presented in Attachment SP-1, page 10 of 10, in Docket No. 3760 are lower in most months than the Bank of America Prime Rate.

The purpose of the interest rate calculations in the Company's gas cost reconciliations is to compensate the Company for the costs of carrying under-recoveries of gas costs. It was not intended to serve as an additional source of profit for the Company. Yet, to the extent the Bank of America Prime Rate exceeds NG's actual short-term debt costs the potential exists for additional unintended profits to be accrued by the Company. In that context, use of the Company's actual cost rates for short-term debt appears to be a more appropriate alternative. The Bank of America Prime Rate could still be used for estimating interest for

prospective DAC costs, but actual short-term rates should be required for use in reconciliation filings.

Q. ARE THE ANY OTHER ALTERNATIVES THAT MIGHT BE CONSIDERED FOR USE IN THE CALCULATION OF INTEREST ON DEFERRED BALANCES IN THE COMPANY'S DAC RECONCILIATIONS?

A. It is my understanding that National Grid currently makes similar interest calculations in its Standard Offer reconciliations using a Customer Deposit Rate that is premised on the costs of 10-year U.S. Treasury Notes. Applying a similar approach to the calculation of interest on deferred gas cost balances might also be an acceptable alternative for prospective application to the Company's GCR reconciliations.

Impacts on Customer Bills

Q. WHAT ARE THE IMPACTS ON CUSTOMERS' BILLS OF THE COMPANY'S PROPOSED DAC?

A. As shown in Attachment PCC-9 to Mr. Czekanski's September 1, 2006 testimony, the impacts of the Company's proposed DAC charge are small. No class would see more than a 0.3% increases in annual billed charges as a result of the proposed change in the level of the Company's DAC charge. Furthermore, when the impacts

of the proposed increase in the DAC charge are considered in combination with proposed reductions in the Company's GCR charges pending in Docket No. 3766, all gas sales service customers would see net reductions in their annual charges for gas service. The combined effects of the Company's pending DAC and GCR rate adjustments are illustrated in Attachment PCC-4 to the testimony of witness Czekanski in Docket No. 3766. Depending on the size and type of customer, those reductions in total charges for sales service customers would generally fall within a range from 2.7% to 5.2%.[2]

Q. DO YOU HAVE ANY CONCERNS REGARDING THE REPRESENTATIVENESS OF THE BILL COMPARISONS THAT THE COMPANY HAS PROVIDED IN THIS PROCEEDING?

A. I do. The "typical" usage levels reflected in Attachment PCC-9 in this proceeding and in Schedule PCC-4 in Docket No. 3766 consistently understate average usage levels for all rate classes. Moreover, for the Residential Non-Heating, C&I Small, and C&I Medium classes, annualized average weather-normalized use per customer for the 12 months ended June 30, 2006 (as indicated in NG's response to Division Data Request 1-3) is greater than the **upper end** of the range of usage shown in the

[2] Attachment PCC-9 to witness Czekanski's September 1, 2006 testimony in this proceeding purports to to compare bills computed using the current GCR and DAC rates with bills computed using the GCR and DAC

Company's bill comparisons. For the Residential Heating class, annualized average weather-normal gas use per customer falls within the range of usage levels for which bill comparisons are computed. But, the annualized average use per customer for that class is 12.5% higher that the level of gas use that the Company represents as typical for such customers. The following table compares the Company's bill comparison range of usage, its represented typical usage, and its reported annualized average weather-normalized use per customer for the 12 months ended June 30, 2006 for Residential and Small and Medium C&I rate classifications.

	Bill Comparison Range	Company Indicated Typical Use	2006 Avg. WN Annual Use/Cust[3]
Residential Non-Heating	115 - 191	153	242
Residential Heating	776 - 1,294	1,035	1,164
C&I Small	932 - 1,553	1,242	1,608
C&I Medium	7,761 - 12,935	10,348	14,304

Thus, one again, I encourage the Company to update its measures of "typical" customer use and expand the ranges of gas use for which bill comparisons are computed. The Company and the Commission should be sensitive to the fact

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rates the Company has proposed for the 2006-2007. However, no changes in GCR charges are reflected in that attachment.

[3] Average weather normalized annual gas use per customer for FY 2006.

that bill comparisons for "typical" customers, particularly for the Residential Heating class, are frequently cited in media reports regarding such rate filings, and therefore, incorrect representations regarding "typical" gas use may distort the rate impact information that is reported to the public.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.